

Computed Value Pre-Assessment Survey

Internal Control Technical Guide

Objective

Provide guidance for performing a Pre-Assessment Survey (PAS) of the company's internal control for computed value and evaluating the results.

Background

Generally Accepted Government Auditing Standards require the PAS team to obtain a sufficient understanding of internal control to plan the audit and determine the nature, timing, and extent of tests to be performed.

The guidelines and terms in this technical guide are based on *Assessing Internal Controls in Performance Audits*, GAO/OP-4.1.4, published by the United States General Accounting Office, Office of Policy, September 1990, and the American Institute of Certified Public Accountant's *Statement on Auditing Standards No. 78*.

19 CFR 152.106(a) defines the computed value of imported merchandise as the sum of:

- (i) the cost or value of materials and the fabrication and other processing of any kind employed in the production of the imported merchandise;
- (ii) an amount for profit and general expenses equal to that usually reflected in sales of merchandise of the same class or kind as the imported merchandise that are made by the producers in the country of exportation for export to the United States;
- (iii) any assist, if its value is not included under paragraph (a) (1) or (2) of this section; and
- (iv) packing costs.

Examples of Red Flags

The following examples are conditions that may indicate a potential problem with the valuation of merchandise under computed value.

- Company has insufficiently documented, poorly defined, or no internal control for accurately declaring value for Customs purposes. Examples:
 - ✓ The company does not monitor or interact with the broker on computed value issues.
 - ✓ The company relies on one employee to handle computed value issues, and there are poor or no management checks or balances over this employee.
 - ✓ The company does not have procedures in place to ensure that material costs are actual and not standard costs.
 - ✓ For computed value involving HTSUS 9802.00.80/90,
 - ◇ The company does not have procedures to ensure that computed value amounts trace to supporting documents.
 - ◇ The company does not have procedures to reconcile reported foreign operating expenses to foreign assembler's income statement.
- Company's import staff lacks knowledge of computed value issues.
- Company offers unreasonable explanations to Customs.
- Company fails to cooperate with or respond to Customs.

- Company has high turnover of people in key positions.
- Consignment merchandise.
- A significant variance exists between total entered value and total computed value.
- Amounts shown on product cost sheets for unallowable costs such as general expenses and profit that are unusually low or nonexistent. [In general, an amount for gross profit (general expenses and profit) of less than 20% of the sales price is low]
- Customs (e.g., import specialist, account manager, compliance measurements, prior audit, other Customs information) shows a history of problems with computed value.
- The company does not maintain and report computed costs in a format that clearly accumulates all dutiable costs.
- Non-manufacturing importer with manufacturing equipment depreciation or credits to fixed asset accounts (unreported assists).
- Chart of accounts indicates dutiable assists that are not reported.
- Use of standard costs without any adjustments for variances.
- For computed value involving HTSUS 9802.00.80/90,
 - ✓ Discrepancies between the foreign assembler's income statement expenses and profits and the expenses and profit reported to Customs.
 - ✓ Allocation basis results in dutiable costs not being proportionally allocated between dutiable and non-dutiable HTSUS.
 - ✓ Non-dutiable material costs are not equal to the HTSUS 9802.

Examples of Best Practices

- Internal controls over computed value:
 - ✓ Are in writing;
 - ✓ Include procedures for monitoring and feedback,
 - ✓ Are monitored by management, and
 - ✓ Mandate that supporting documents for summary computed value documents are clearly identified and retained.
- One manager is ultimately responsible for control of the Import Department, including ensuring merchandise is properly valued. That manager has knowledge of Customs matters and the authority to ensure that internal control procedures for imports are established and followed by all company departments.
- Written internal control procedures assign Customs related duties and tasks to a position rather than a person.
- Company has good interdepartmental communication about Customs matters.
- Company conducts and documents periodic reviews of computed value, and uses the results to make corrections and changes to their import operations as appropriate.
- Current standard costs are used to value imported merchandise at time of entry.
- The General Ledger system is designed to identify the value and dutiable status of all merchandise purchased for consignment to the foreign assembler.
- The General Ledger system is designed to identify all dutiable assists.
- For computed value involving HTSUS 9802.00.80/90,
 - ✓ The foreign assembler's cost accounting system allocates overhead and General and Administrative (G&A) expenses and profit to products in a reasonable manner.
 - ✓ The foreign assembler compares its rates for profit and general expenses (gross profit) to industry rates in the country of export, and uses industry rates if there are significant differences.

- ✓ The company calculates computed value using a format that accumulates all reportable costs

Examples of Documents and Information to Review

- Internal control policies and procedures.
- The company's response to the questionnaire.
- Interviews with company staff concerning actual procedures and controls specific to computed value.
- Documentation that supports monitoring and verification of established and/or written internal control for computed value.
- Documentation that support the computed value such as worksheets showing the calculation and product allocation of overhead, general expenses and profit, financial statements, general ledger, foreign tax reports, and supporting schedules.
- Other documents affecting computed value such as reports of industry rates for gross profit (general expenses and profit) in the country of export, purchase orders, contracts, agency agreements, and risk sharing agreements.

Suggested Testing

PAS team judgement should be used to determine the type and amount of testing needed to evaluate how effective internal control is and whether there is a sufficient risk to warrant proceeding to the Assessment Compliance Testing (ACT) process.

Using the chart and guidelines below, determine through limited judgmental testing whether the company's internal control is effective.

To determine the extensiveness of internal control testing, it is necessary to evaluate:

1. The **risk exposure**, and
2. The **internal control** system, by determining if the controls are in operation, how the controls are applied, how consistently they are applied, and who applies them.

Risk Exposure

Risk exposure is the probability of significant Customs noncompliance. In each step of determining risk exposure, consideration should be given to:

1. Significance (to Customs) and sensitivity (e.g., issues of interest to Congress or the media, or impacting admissibility).
2. Susceptibility (of making incorrect declarations).
3. The existence of any "red flags."
4. Management support (of strong internal control).
5. Competent personnel (to adequately administer the controls).

Steps to Determine Risk Exposure:

1. Evaluate problems identified in the profile, compliance measurement rates, questionnaire, and concerns raised by the import specialist and account manager.
2. Perform the macro risk analysis test.
3. Analyze all results to determine the risk exposure level.
4. Evaluation of risk exposure is not simply a one-time process that occurs at the start of the PAS process. Continually reassess risk exposure as more information is gathered from evaluating internal control and performing other work in the PAS.

Macro Risk Analysis Examples*Example A: Low Risk Exposure*

The Importer's cost of goods manufactured closely approximated the entered value for the period under review. Rates used by the foreign assembler for general expenses and profit (gross profit) were comparable to industry standards. Additionally, review of the profile and discussions with the Import Specialist and Account Manager did not reveal any special concerns. Therefore, the macro risk analysis indicated a low risk exposure.

Example B: High Risk Exposure

Based on a review of the completed questionnaire, it was determined that the importer may not have included certain general ledger expenses in the calculations of actual dutiable value. The PAS team conducted interviews with the company's key financial accounting personnel and determined that the company did not include all depreciation expense on equipment assigned to the company's foreign affiliate in the calculation of actual dutiable value. The PAS team compared depreciation expense on the actual dutiable computation worksheet in the amount of \$1,758,595 to the annual totals for general ledger account numbers 10000 through 10999 (depreciation expense - foreign) in the amount of \$5,658,587. Based on this analysis the PAS team determined that the actual dutiable value could be understated by as much as \$3,899,992 (\$5,658,587-\$1,758,595), representing 2 percent of the companies estimated entered value for the review period. In addition, the company's Summary of Customs duty paid indicated that duty rates ranged from 1.2 percent to 5.7 percent. Therefore, the macro risk analysis indicated a high risk exposure.

System of Internal Control

To evaluate the internal control system:

1. Consider the five components of internal control:
 - Control Environment.
 - Risk Assessment.
 - Control Activities.
 - Information and Communication.
 - Monitoring

2. Review relevant Customs and company documents to identify and understand relevant internal control over computed value. (Examples of documents and information to review are listed above.)
3. Determine whether the company established and follows procedures. Review:
 - Documentary evidence of the results of periodic internal control reviews/testing and corrective action implemented.
 - Documentary evidence of communication between the broker and company on value issues, company testing of broker operations and verification that the broker followed company instructions.
 - Company-specific rulings and evidence that they are followed.
 - Documentary evidence of intra-company communications to ensure correct information is provided to Customs.
 - Training records and materials used to educate staff on Customs matters.
 - Evidence, such as a log, that demonstrates the company periodically reviews broker's or the company's values.
 - Evidence that standard costs are periodically reviewed and updated.
 - Evidence that rates used for general expenses and profit (gross profit) are comparable with the industry rates.
4. Review written policies and procedures and interview applicable company personnel to complete appropriate sections of the "Worksheet for Evaluating Internal Control Over Computed Value."

Note: The internal control assessment should include steps to:

- Identify and understand internal control.
- Determine what is already known about control effectiveness.
- Assess the adequacy of internal control design.
- Determine whether controls are implemented and effective.
- Determine whether transaction processes are documented.

Extensiveness of Audit Tests (Testing Limit)

The purpose of limited PAS testing is to take a survey in order to determine the necessity for and extent of substantive tests. In some circumstances, the PAS team may decide that it probably will not be able to form an opinion based on limited PAS testing. In that case, it may be necessary to proceed immediately to the ACT process. If the PAS team believes that it can form an opinion based on limited PAS testing, test the appropriate number of controls and associated transactions using the table below.

Determine Extensiveness of Audit Tests

Risk Exposure	+	Preliminary Review Internal Control	=	Extensiveness of Audit Test	Testing Limit
High		Weak Adequate		High Moderate to High	10-20

Risk Exposure	+	Preliminary Review Internal Control	=	Extensiveness of Audit Test	Testing Limit
		Strong		Low to Moderate	
Moderate		Weak		Moderate to High	5-15
		Adequate		Moderate	
		Strong		Low	
Low		Weak		Low to Moderate	1-10
		Adequate		Low	
		Strong		Very Low	

Source: Adapted from *Assessing Internal Controls in Performance Audits*.
Column titled "Testing Limit" reflects Customs test sizes.

Evaluation of Pre-Assessment Survey Testing Results

The following steps are guidance for determining the effectiveness of company's internal control over computed value.

- Complete the "Worksheet for Evaluating Internal Control Over Computed Value" to determine whether risk determination is acceptable or unacceptable and document why. Put the results of testing in perspective and evaluate confirmed weakness as a whole. The evaluation should consider the results of the internal control testing, problems identified in the profile, and/or concerns raised by the import specialist and account manager. The team must evaluate the PAS results based on the specific situations.
Customs considers risk unacceptable when testing reveals that internal control is not effective, or not sufficient, in providing reasonable assurance that accurate, timely, and complete declarations are reported to Customs.
- The following will assist the PAS team in determining whether conditions warrant proceeding to ACT:
 - Do not proceed to ACT (Revenue) if:**
 - ✓ Cost-benefit analysis warrants no further effort (do not spend a significant amount of resources to identify a potential loss of revenue considered insignificant).
 - ✓ The PAS indicated that the value error was due to an isolated incident.
 - ✓ The company agrees with PAS finding(s) and agrees to quantify the loss of revenue within an acceptable timeframe.
 - Do not proceed to ACT (Compliance) if:**
 - ✓ The error was isolated.
 - ✓ The errors were systemic and the importer agreed to develop and implement a compliance improvement plan within an acceptable timeframe.
 - Proceed to ACT (Revenue) if:**
 - ✓ Company does not have adequate internal control, and PAS indicates a material loss of revenue that cannot be quantified without statistical sampling or further review.
 - ✓ Importer will not quantify loss of revenue.

- **Proceed to ACT (Compliance) if:**

- ✓ The company refuses to take corrective action on systemic errors and it is necessary to calculate a compliance rate.

Note: If substantive tests necessary to determine a compliance rate or revenue loss can be quickly performed without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

3. Determine whether referrals should be made for enforcement action.

Examples

The following examples of situations that might be encountered under PAS *are for clarification only*:

Example A: Situation in which the team would not proceed to ACT (Revenue)

Company's Policies and Procedures

The company procedures requires that general ledger account transaction detail be downloaded by the foreign subsidiary and provided by the accounting department, to the Compliance Manager within 30 days of the end of each fiscal year. The Compliance Manager (Import Manager) and two Compliance Analysts review the chart of accounts and select all manufacturing expense accounts and appropriate non-manufacturing accounts (i.e. general operating expenses) for inclusion in the calculation of actual dutiable value (ADV). Once the dutiable accounts are identified, the Compliance Analyst prepares ADV worksheets using general ledger account transaction detail after year-end adjustments are made to standard costs by the accounting department. Standard costs are evaluated every year and are based on the results of the most recently completed annual computed value. Additionally they compare rates used by the foreign assembler for general expenses and profit (gross profit) to industry rates, and use industry rates if there are significant differences.

The company calculates computed value using a format that accumulates all reportable costs. The company calls the report an Actual Cost Report (ACR). Once the ACR is prepared, it is reviewed and signed by the Accounting Manager and the Import Manager. The ACR and supporting schedules and EDP files are filed and maintained by the Import Manager. The Accounting Manager maintains another backup copy.

Differences in estimated and actual entered values are applied to estimated entered values by HTS on schedules prepared by the company's broker in order to determine additional duties due. The Customs broker makes the value allocation based on a ratio of the entered values per HTS to the total entered value for the year. The broker's calculation's are reviewed and signed by the Import Manager and the broker then files the appropriate reconciliation entry. On an annual basis, the company's internal audit department reviews the cost preparation process, and makes appropriate recommendations as needed.

Monitoring Activities

The Import Compliance Manual established procedures to ensure that values of entered merchandise were accurately reported to Customs. First, the Import Manager and two Compliance Analysts review the chart of accounts and select all manufacturing expense accounts and appropriate non-manufacturing accounts for inclusion in calculating actual dutiable value. Detailed evaluations of new accounts are conducted with the assistance of the Assistant Controller. In addition, the process of calculating the actual costs is documented in a permanent file that is reviewed and signed by the Import Manager and Accounting Manager.

Ratios between the last years estimated and actual costs are compared to the current year ratios for purposes of testing the reasonableness of actual values. The Import Manager and Accounting Manager review the broker's calculations of duties due, and indicate their review by signing each of the broker's worksheets.

Finally, the manual establishes procedures for conducting internal audits on an annual basis. The manual requires that the Import Manager review a sample of 5 transactions from 10 accounts not used in the preparation of actual cost, in order to determine if some of the account transactions should be included in the actual dutiable value. The accounts and the sample items are to be randomly selected.

The Import Manager holds a meeting prior to the preparation of the current ACR, in order to educate those involved in the preparation process of issues or concerns identified in prior years. All meetings, training seminars and discussions regarding the process are documented and filed by the Import Manager. In addition, employees involved in the process of preparing costs for Customs value attend a one-week training session provided by the company's outside counsel.

Pre-Assessment Survey

To determine if the controls were working, the PAS team:

- Interviewed employees engaged in the preparation of ACR's to determine if they were familiar with the procedures established in the Customs Compliance Manual.
- Verified that the trial balance included all general ledger transactions.
- Verified the ACR review process and that they were signed by the Accounting Manager and the Import Manager.
- Selected 10 of the 50 transactions not used in the preparation of actual cost and reviewed by the Import Manager to verify how the review had been conducted.
- Reviewed broker duty calculations to ensure that they were reviewed.
- Compared brokers estimated duty to the PAS teams estimated duty totals.
- Reviewed internal audit reviews of the last two years ACR reviews.
- Reviewed attendee sign-in sheets and course descriptions for periodic training sessions regarding preparation of ACR's.
- Reviewed correspondence between the company and Customs on value related matters.

The PAS indicated that the company's internal controls were in affect and were working with one exception. One dutiable account was omitted from the calculations used to calculate dutiable costs and file the reconciliation entry. The company agreed to file corrective entries to report the additional value and to pay the additional duty. Therefore proceeding to ACT was not considered necessary.

Example B: Situation in which the team would not proceed to ACT (Compliance)

Same situation as Example A above. The company agreed to change procedures to include the account in the future. Therefore, it was not necessary to proceed to ACT to calculate a rate for compliance.

Example C: Situation in which the team would proceed to ACT for (Revenue)

Same situation as Example A above, except unreported assists were identified in a material account. Statistical sampling was necessary to separate dutiable assists from material that was used in domestic production.

Example D: Situation in which the team would proceed to ACT (Compliance)

The same situation as Example A above, with the additional finding that the Import department had decided that reviewing all the new general ledger accounts was too cumbersome due to the company's change in accounting system that had occurred early in the audit period. In addition, the company did not agree to take proper corrective action. Proceeding to ACT was considered necessary due to the fact that there were many general ledger accounts not yet reviewed that could impact the ACR.

Worksheet for Evaluating Internal Control

Over Computed Value Objective: Determine whether the company has procedures designed to effectively control Customs risks related to computed value.

Risk Determination:

Acceptable _____

Unacceptable _____

Internal Control	Yes	No	Not Applicable	Internal Control Manual Page Number	Work Paper Reference	Comments
Are internal controls over computed value formally documented?						
Are written policies and procedures approved by management?						
Are written policies and procedures reviewed and updated periodically?						
Are internal controls over computed value periodically tested?						
Were the results of the periodic internal control tests documented?						
If weaknesses were found during internal control testing, were import operations corrected?						
Were results of periodic tests used to file corrections to Customs declarations when appropriate?						
Do written internal control procedures assign computed value responsibility to a position rather than an individual?						

Internal Control	Yes	No	Not Applicable	Internal Control Manual Page Number	Work Paper Reference	Comments
Is one department/individual primarily responsible for ensuring compliance with computed value requirements?						
Does the individual overseeing compliance with computed value requirements have adequate knowledge and training and authority to ensure that internal control procedures for imports are established and followed by all company departments?						
Does the company have good interdepartmental communication about value matters?						
Do procedures ensure that industry rates for general expenses and profit (gross profit) in the country of export are checked, and used if significantly different than company rates?						
Do procedures ensure that, if standard costs are used, variances are added to arrive at actual costs?						
Do procedures ensure that material costs include transportation costs to the place of production?						
Do procedures ensure that freight costs are properly allocated between dutiable and non-dutiable materials?						

Internal Control	Yes	No	Not Applicable	Internal Control Manual Page Number	Work Paper Reference	Comments
Do procedures ensure that materials are properly identified between dutiable and non-dutiable tariff numbers?						
Do procedures ensure that dutiable costs are not allocated to non-dutiable tariff numbers?						
Do procedures ensure that any internal tax imposed on imported material by the country of exportation, which is refunded at the time of exportation, are excluded from material value?						
Do procedures ensure that all foreign operating expenses, applicable to the production of exported merchandise, and profit reported on the foreign assembler's income statement are reported as part of computed value.						
Do procedures ensure that exchange gains are reported and that translation gains are not reported as part of computed value?						
Do procedures ensure that all assists are included?						
Do procedures ensure that material scrap value, less any proceeds from the sale of the scrap, is included in computed value?						
Internal Control Conclusions						

Internal Control	Yes	No	Not Applicable	Internal Control Manual Page Number	Work Paper Reference	Comments
Does the company provide adequate broker oversight?						
Did PAS testing verify that control procedures were being followed?						
Did interviews with responsible persons support control procedures?						
Does the company have adequate internal control to address specific issues identified in the profile?						
List company-specific procedures and controls below (if applicable)						